STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2000-140

April 28, 2000

NORTHERN UTILITIES, INC.,
Proposed Cost of Gas
Factor for the 2000
Summer Period and Annual
Environmental Recovery Cost
Adjustment

ORDER

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

We approve Northern Utilities, Inc.'s (Northern) proposed Cost of Gas Factor (CGF) for the 2000 summer period and an Environmental Response Cost Adjustment (ERCA) of ($0.0175) per Ccf. We require Northern to include with its August 2000 CGF filing an explanation for the recent variances between forecasted sales and actual sales that may result from forecast model inaccuracies.

II. PROCEDURAL HISTORY

On February 24, 2000, pursuant to 35-A M.R.S.A. § 4703 and Chapter 430(2) of the Commission's Rules, Northern filed its proposed CGF for the Summer 2000 gas usage period as well as its proposed change to the ERCA as allowed in Docket No. 96-678. The Commission issued a Notice of Proceeding to interveners in prior CGA cases and by publication in newspapers of general circulation in Northern's service area.

The Office of the Public Advocate (OPA) intervened. To investigate the proposed CGF changes, the Advisory Staff and OPA issued data requests to the Company on its filing. A preliminary hearing was held on April 4, 2000 at which the Advisory Staff explored the issues raised by this filing. In addition, the Hearing Examiner established a schedule for the remainder of this proceeding that included allowing Northern to update its filing and issued a proposed order for parties' comment prior to deliberations.[1]

On April 10, 2000, Northern filed a revision to its CGF filing incorporating an updated forecast of summer period commodity costs. This update increased the proposed CGF rates by an average of approximately 3 cents per therm.

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[1] At the April 4, 2000 conference, the Examiner allowed the OPA additional time, until April 7, 2000, to indicate any other issues beyond those discussed by the Advisory Staff that it wished to pursue in this case. We received no notification and conclude that the OPA raises no further issues in this case.

The Advisory Staff issued a proposed order recommending approval of Northern's proposed CGF on April 13, 2000.

III. RECORD

The record in this proceeding includes all filings, data responses, transcripts, and any other materials provided in this proceeding.

IV. DISCUSSION

A. Overview of Proposed Rates

This is Northern's first Summer CGF filing reflecting the rate design changes approved in *Northern Utilities, Inc., Request for Approval of Rate Design and Partial Unbundling Proposal,* Docket No. 97-393, Part One Order Approving Stipulation (Sept. 3, 1999). One of the major changes is that the CGF is now calculated on a class-specific basis instead of on a company-wide basis. Northern proposes the following 2000 Summer Period CGF rates on a per hundred cubic feet (Ccf) basis to become effective May 1, 2000:

Class	**Rate**
Residential - Heat & Non-Heat (R-2 & R-1)	$0.5187
Small Commercial - Low Winter Use (G-50)	0.4925
Small Commercial - High Winter Use (G-40)	0.5125
Medium Commercial - Low Winter Use (G-51)	0.4967
Medium Commercial - High Winter Use (G-41)	0.5018
Large Commercial/Industrial – Low Winter Use (G-52)	0.4955
Large Commercial/Industrial – High Winter Use (G-42)	0.4866

The filing also includes a revised ERCA of ($0.0175) for the summer period from the ERCA rate of ($0.0091) in effect in the 1999/2000 Winter CGF. The revision is calculated to reflect the difference between the estimated and actual ERC recoveries made during the winter period.

The issues related to these proposed rates are discussed separately below.

B. Issues

1. Rate Design Changes

We recently approved a revised rate design for Northern that establishes specific gas commodity rates for each customer class rather than assigning a single, average CGF to all classes. See *Northern Utilities, Inc., Request for Approval of Rate Design and Partial Unbundling Proposal*, Docket No. 97-393, Order (Sept. 3, 1999). In addition, the rate design modified the classes and membership to better match the cost of providing service. Finally, this CGF includes gas-related portions of revenue requirements, such as working capital and bad debt expense, that were moved from base rates to the CGF. The overall effect of this rate design was an increase in residential customers' gas rates and decreases in the gas rates for large industrial customers. Some customers will also experience bill impacts from changes to the customer classes.

Our Advisory Staff has reviewed Northern's proposed Summer 2000 CGF rates and concludes that they appear consistent with the recently approved rate design stipulation.

2. Last Summer Period Under-collection

On February 17, 2000, Northern reported an under-collection from the last summer period of approximately $822,626. Northern states that this under-collection resulted from a combination of greater than forecasted gas costs and less than forecasted gas sales. Actual sales were 1,490,653 Ccf less than forecasted.

Maine regulatory law allows for the recovery of prior period cost of gas under-collections, with interest, during the next corresponding seasonal period. 35-A M.R.S.A. § 4703 and Chapter 430 of the MPUC Rules. Accordingly, the Summer 1999 under-collection increases the proposed Summer 2000 period unit cost of gas by approximately 3.5 cents per therm.

3. Modified Gas Cost Estimating Methodology

In this filing, Northern modified the manner in which it estimated its commodity costs for the upcoming CGF period. Previously, Northern based its cost estimates for Canadian supplies on the most recent twelve-month's experience of its

Canadian purchases. In its current filing, Northern uses the New York Mercantile Exchange (NYMEX) futures price for gas as reported in the Wall Street Journal as an additional determinant for estimating its commodity costs. Specifically, Northern estimates its cost of gas for particular contracts based on the average differential between the historical NYMEX and the historic actual prices for that particular gas supplier over the past two years. Northern believes that using the average differential between historical NYMEX gas futures and actual historical prices will allow its estimates to be more accurate.

Oil and gas prices have fluctuated widely in recent history. Northern submits that this gas cost estimation method will better anticipate gas market price changes. If so, its use should improve the accuracy of Northern's gas cost estimates resulting in reduced under- and over-collections for carry over into future rate periods, giving better price signals to customers.

We note that estimating future period gas costs is inherently speculative. Gas cost adjustment mechanisms are designed to allow the Company to recover its actual costs, anticipating that estimated costs will not accurately match actual costs. The fact that the CGF reconciles estimated to actual price differences automatically corrects any errors that exist in any particular estimation methodology. We must review this proposed methodology to determine only that it is reasonable.

We conclude that Northern's proposed gas price estimation methodology appears to be likely to more accurately predict future price changes that will be passed on to its customers and, we find it to be a reasonable method for setting this summer's CGF. We will review the performance of this new approach in future CGFs to ensure that it produces reasonable results.

4. Forecasting Variances

During our review of the current CGF filing, as well as several recent ones, Advisory Staff noted that Northern has previously had large over- and under-collections as a result of variances between its forecasted and actual sales. Northern believes that the major reason these variances exist is that its forecasting model did not reflect a recent period of expansion curtailment and, as a result, has improperly estimated growth. However, Northern states that it has not thoroughly investigated this premise to determine if its belief is accurate or if the variances may instead result from errors or deficiencies in its forecasting model.

We are concerned about the trend not only because of the large over/under-collections that it produces but also because of the potential impact on Northern's overall cost of gas. If Northern is forecasting unrealistically high sales volumes, then it could be subscribing to excess pipeline capacity and commodity gas, unnecessarily inflating its overall gas costs. Conversely, an unrealistically low gas demand forecast could result in insufficient pre-subscribed pipeline capacity or gas, requiring expensive spot market purchases. In either case, the cost of gas to the ratepayers could be too high.

At Advisory Staff and OPA's request, Northern agreed to review its forecast model to determine the cause of its recent forecasting errors and to include the results of that investigation in its 2000-2001 Winter CGF filing. If Northern finds that its model is not operating in a manner that produces accurate results, it should also include its proposal for correcting the model in that filing.

5. Environmental Response Cost Adjustment (ERCA)

Northern has revised its ERCA rate by spreading unrecovered environmental remediation costs allowed in this recovery period over its projected sales for the upcoming summer period. We find that the proposed ERCA is consistent with the summer period adjustment methodology approved in Docket No. 96-678, and we approve it.

V. CONCLUSION

The combination of the initial implementation of summer period rate design changes, substantial increases in projected gas prices, and a large under-collection in the prior summer period results in higher summer CGF rates for certain classes than is typical historically. In some cases, we note that these factors have produced summer gas cost rates for a few classes that are slightly higher than the current winter rates.

However, it appears that these anomalies result from unique circumstances that include markedly higher market prices for natural gas, rate design changes, and a prior period under-recovery. This particular mix of circumstances is not expected to recur. Our Advisory Staff has reviewed the underlying reasons for these proposed rates and recommends their approval. Thus, though anomalous, we find no cause to reject the current proposed rates.

Accordingly, we

O R D E R

1. That Northern Utilities, Inc.'s proposed revised CGF rates shall take effect for gas consumed on or after May 1, 2000;

2. That Northern Utilities, Inc.'s Thirty-second Revised Sheet No. 20.1 constituting its Cost of Gas Factor for the period May 1, 2000 through October 31, 2000, is approved;

3. That Northern Utilities, Inc.'s Seventh Revised Sheet No. 34.3, the Environmental Response Cost Adjustment tariff, is approved and will become effective May 1, 2000;

4. That Northern Utilities, Inc.'s shall include in its 2000-2001 Winter CGF filing a discussion and explanation of the reasons for the forecasting errors noted herein.

Dated at Augusta, Maine, this 28th day of April, 2000.

BY ORDER OF THE COMMISSION

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Raymond J. Robichaud
Acting Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Civil Procedure, Rule 73, et seq.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.